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Can Lynn, 38, and Wyatt, 31, afford to move their family to a better school district?

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With two small children, Lynn and Wyatt are thinking of moving from their modest Toronto-area house to a larger one in a better school district.

Lynn is 38, Wyatt is 31. The children are 3 and 5.

"We've been running the numbers for over a year now, looking at what we could afford," Lynn writes in an e-mail. "We secured higher-paying jobs and got preapproved by our bank for a higher mortgage," she adds.

In her new public-health job, Lynn will be making $110,000 a year. She'll have a defined-benefit pension plan to which both she and her employer contribute. Wyatt makes $122,000 a year and has a defined-contribution pension plan. Only his employer has the obligation to make contributions. Wyatt can still contribute, but it is optional.

They would sell their existing house and buy a larger one for about $1.5-million. They'd have to put saving on hold for the first two years as they renovate the new house and buy a used car. Their concern is that taking on a larger mortgage might interfere with their ability to retire at the age of 65.

How much will they have to save over their working lives to live comfortably and maintain their standard of living when they retire?

We asked Ian Calvert, a certified financial planner and principal at HighView Financial Group in Toronto, to look at Lynn and Wyatt's situation.

WHAT THE EXPERT SAYS

Lynn and Wyatt have clearly defined short and long-term goals, Mr. Calvert says. "Their top priority in the short run is upgrading their house for their two children – without jeopardizing their retirement." They've already given some thought to a pretax retirement spending goal – $150,000 a year – although this is still many years in the future. "Planning this far into the future is an impressive achievement," the planner says. Identifying a longer-term target, even if it is an estimate, will allow for more precise planning today.

Upgrading to a larger house will result in two material financial changes, Mr. Calvert says: the upfront costs of the move and the higher carrying costs. "The largest initial expense will be the land transfer tax due upon closing." In Toronto, there will be provincial and municipal land transfer taxes totalling $52,920, he says.

They have a mortgage of $506,000, which will increase by $300,000 after the purchase of their new property. "They should expect a new monthly mortgage payment of about $4,400 a month, $1,400 higher than their current payments," the planner says. These costs, plus renovations to their new house, will force Lynn and Wyatt to use existing savings and put their future savings on hold for two years.

"Taking two years off from saving anything can certainly be disruptive to a retirement accumulation," the planner says. Because they have a long runway of 27 more working years ahead of them, they certainly have time to catch up, he says. They will still be reducing their mortgage debt and marginally increasing their equity during the years of little to no savings.

Once they are settled in their new home, re-establishing annual saving targets should be a top priority, Mr. Calvert says. Lynn has a small defined-benefit pension of $8,780 a year from a previous employer. In her current job she has a public-sector defined-benefit pension plan, so her annual pension adjustment will significantly reduce her ability to save in her registered retirement savings plan. (The pension adjustment lowers the amount she can contribute to her personal RRSP.)

Lynn should aim for a full contribution to a tax-free savings account as her top priority. Once the TFSA is maxed out, she could consider a small RRSP contribution. The TFSA will set her up for greater flexibility in the long run as it will be a pool of tax-free money.

Wyatt has a small defined-benefit pension from a previous job that will pay about $2,400 a year at retirement, in addition to his current defined-contribution plan. This creates a pension adjustment for the amount of the employer contributions, the planner says. For this type of plan, the value will depend on the management of the underlying retirement assets.

"Wyatt should still aim for personal RRSP contributions each year," Mr. Calvert says.

Wyatt should also aim for a maximum TFSA contribution, but there is a greater motivation to contribute to his personal RRSP because he won't have the same level of guaranteed retirement income as Lynn.

Currently, they have a portfolio that is mostly exchange-traded funds. They have a 90-per-cent equity exposure with a stronger tilt to U.S. stocks. This is an effective method to gain exposure to many stocks at a low cost without considering individual security selection, the planner says.

"As most ETFs are designed to track, not beat, the market, it's important not to actively trade them because they are passive investment products," Mr. Calvert says. "Staying disciplined, not selling into volatility, and adding capital at optimal entry points will be crucial for this type of portfolio over the long run."

They have a pretax spending target of $150,000 a year. Because retirement is many years away, they should be considering an inflation-adjusted target. "With an annualized average inflation adjustment of 2 per cent, they should really be planning for a $250,000 target at age 65."

When both are 65, their retirement income might have the following components: Future estimated Canada Pension Plan benefits of $27,000 each, estimated Old Age Security of $17,000 each, and Lynn and Wyatt's combined work pension income of $100,000 a year. This would leave a gap of $62,000. If Lynn and Wyatt both contributed $7,000 each to their TFSAs starting in 2027, and earned on average 5 per cent a year, they would have a combined value of more than $1-million in tax-free assets, Mr. Calvert says. Furthermore, Wyatt's defined-contribution plan is expected to be $685,000. Drawing $62,000 a year from a portfolio of $1,685,000 would be a sustainable 3.7-per-cent withdrawal rate.

"The combined total of their retirement assets should put them in a position to fund their retirement gap without encroaching on their underlying capital," the planner says.

CLIENT SITUATION

The people: Lynn, 38, Wyatt, 31, and their two children, 3 and 5.

The problem: Can they move to a larger house without jeopardizing their retirement goals?

The plan: Because she has a defined-benefit pension, which eats into her RRSP room, Lynn should focus first on her TFSA. Wyatt should contribute to a personal RRSP to supplement his defined-contribution pension. Contributing the maximum to their TFSAs each year will help ensure they meet their savings goal.

The payoff: A better idea of how much they have to save – and how much they can spend – over the years until they are both retired.

Monthly net income: $12,735.

Assets: Bank accounts $7,475; her TFSA $175; his TFSA $6,455; her RRSP $30,525; his RRSP $30,045; registered education savings plan $20,470; residence $1,200,000. Total: $1.3-million. Estimated present value of her two DB pensions $1,420,000. Estimated present value of his DB pension $125,000. Those amounts combined are what someone with no pension would have to save to generate the same income.

Monthly outlays: Mortgage $3,275; property tax $315; water, sewer, garbage $165; home insurance $165; electricity $120; heating $105; security $10; maintenance $125; transportation $390; groceries $1,200; child care $1,940; clothing $200; line of credit $300; gifts, charity $150; vacation, travel $310; miscellaneous unallocated spending $1,246; dining, drinks, entertainment $110; personal care $10; club membership $20; sports, hobbies $45; subscriptions $25; health care $65; phones, TV, internet $125; RRSP $125; registered education savings $210; pension plan contributions $1,745. Total: $12,500.

Liabilities: Mortgage $506,000 at 5.38 per cent; line of credit $39,000 at 5.42 per cent. Total: $545,000.

Ian Calvert is a Vice President & Principal at HighView Financial Group.